



DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

[Docket No. FR-5875-N-01]

Single Family Mortgage Insurance: Revision of Section 203(k) Consultant Fee Schedule - Solicitation of Comment

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Notice; Solicitation of Comment.

SUMMARY: The Section 203(k) Program is HUD's primary program for the rehabilitation and repair of single family properties. The Section 203(k) mortgage program enables homebuyers and homeowners to finance the purchase, or refinance of a home and include the rehabilitation costs through a single mortgage. There are two types of 203(k) rehabilitation mortgages: Standard 203(k) and Limited 203(k).

The Standard 203(k) mortgage may be used for remodeling, rehabilitation and repairs that may have structural components, involve more complex work and the total rehabilitation costs must be greater than \$5,000. The Limited 203(k) mortgage may only be used for minor remodeling and non-structural repairs. The total rehabilitation cost may not exceed \$35,000 and there is no minimum cost.

As part of the Section 203(k) program requirements, the Federal Housing Administration (FHA) maintains a list of approved 203(k) Consultants on the FHA 203(k) Consultant Roster in FHA Connection. An FHA-approved 203(k) Consultant is required for all Standard 203(k) mortgages. A 203(k) Consultant is not required under the Limited 203(k) program, but may be used. FHA-approved 203(k) Consultants are required to perform responsibilities during the

processing and rehabilitation phase of the 203(k) program. FHA-approved 203(k) Consultants who are placed on FHA's 203(k) Consultant Roster are deemed qualified to complete these duties and therefore permitted to collect a fee for this service. In 1995, HUD issued its current Section 203(k) Consultant Fee Schedule and now seeks to update the Section 203(k) Fee Schedule to align with similarly performed services and the corresponding fees collected for such services. As a result, this notice seeks public comment on revising the current structure of the fee and the maximum amount of fees a 203(k) Consultant would be permitted to charge on a Section 203(k) mortgage.

DATES: Comment Due Date: **[INSERT DATE THAT IS 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER.]**

ADDRESSES: Interested persons are invited to submit comments regarding this notice to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500.

Communications must refer to the above docket number and title. There are two methods for submitting public comments. All submissions must refer to the above docket number and title.

1. Submission of Comments by Mail. Comments may be submitted by mail to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500.

2. Electronic Submission of Comments. Interested persons may submit comments electronically through the Federal eRulemaking Portal at www.regulations.gov. HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments

submitted electronically through the www.regulations.gov website can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

Note: To receive consideration as public comments, comments must be submitted through one of the two methods specified above. Again, all submissions must refer to the docket number and title of the notice.

No Facsimile Comments. Facsimile (fax) comments are not acceptable.

Public Inspection of Public Comments. All properly submitted comments and communications submitted to HUD will be available for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Due to security measures at the HUD Headquarters building, an appointment to review the public comments must be scheduled in advance by calling the Regulations Division at 202-708-3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number via TTY by calling the Federal Relay Service at 1-800-877-8339 (this is a toll-free number). Copies of all comments submitted are available for inspection and downloading at www.regulations.gov.

FOR FURTHER INFORMATION CONTACT: Kevin L. Stevens, Director, Home Mortgage Insurance Division, Office of Single Family Program Development, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Room 9266, Washington, DC 20410-9000, telephone number 202-402-4137 (this is not a toll-free number). Persons with hearing or speech impairments may access this number by calling the Federal Relay Service at 800-877-8339 (this is a toll-free number).

SUPPLEMENTAL INFORMATION:

I. Background

Section 203(k) of the National Housing Act (12 U.S.C. 1709(k)) authorizes HUD to insure a purchase or a refinance mortgage on an existing 1-4 unit single family structure and include the rehabilitation costs through a single mortgage. The Section 203(k) Program is HUD's primary program for the rehabilitation and repair of single family properties. The Section 203(k) program is important for neighborhood revitalization and homeownership opportunities. The regulations implementing the Section 203(k) Program are codified at 24 CFR 203.50.

The Section 203(k) Program fills a unique and important role for homebuyers. In the conventional loan market, a homebuyer who purchases a home that is in need of repair or modernization usually has to follow a complicated and costly process. The homebuyer must obtain financing to purchase the dwelling, additional financing for the rehabilitation work, and a permanent mortgage after rehabilitation is completed to pay off the interim loans. The interim acquisition and improvement loans often have relatively high interest rates and short repayment terms. The Section 203(k) Program addresses this by permitting a homebuyer to obtain a single loan, at a long-term fixed or variable rate, to finance both the acquisition and rehabilitation of the property.

There are two types of 203(k) rehabilitation mortgages: Standard 203(k) and Limited 203(k). The Standard 203(k) mortgage may be used for remodeling, rehabilitation and repairs that may have structural components involve complex work and must have a total rehabilitation costs greater than \$5,000. The Limited 203(k) mortgage may only be used for minor remodeling and non-structural repairs, the total rehabilitation cost may not exceed \$35,000 and there is no minimum rehabilitation cost.

The extent of the rehabilitation covered by the Section 203(k) mortgage may range from relatively minor to virtual reconstruction. For example, a home that will be demolished as part of rehabilitation is eligible, provided that the existing foundation remains in place. In addition to typical home rehabilitation projects, the Section 203(k) Program can be used to convert a property of any size to a one- to four-unit dwelling. Section 203(k) mortgage insurance can also be used to augment Energy Efficient Mortgages, Section 203(h) Mortgage Insurance for Victims of a Presidentially-Declared Major Disaster Area, and Mortgage Insurance for Solar and Wind Technologies. All improvements, renovations, or repairs undertaken with Section 203(k) mortgage insurance must comply with the HUD Minimum Property Requirements, HUD Minimum Property Standards and all local codes and ordinances.

II. Section 203(k) Consultants

An FHA-approved 203(k) Consultant is required for all Standard 203(k) mortgages and may be used for Limited 203(k) mortgages. As part of the Section 203(k) program requirements, the Federal Housing Administration (FHA) maintains a list of approved 203(k) Consultants on the FHA 203(k) Consultant Roster from which the Mortgagee must select a 203(k) Consultant and assign the 203(k) Consultant to the transaction, if required.

When a Section 203(k) Consultant is required, the Consultant will enter into a written agreement with the Borrower that outlines the services that the Consultant will perform. In some cases, the Mortgagee or Borrower may require the Consultant to conduct a Feasibility Study to determine if the 203(k) mortgage is achievable, based on the costs of the rehabilitation project. The 203(k) Consultant conducts a Feasibility Study by completing a preliminary inspection of the property, and estimates the material and labor costs for the project.

The 203(k) Consultant must inspect the property to ensure:

- there are no rodents, dry rot, termites and other infestation the property;
- there are no defects that will affect the health and safety of the occupants;
- there exists adequate structural, heating, plumbing, electrical and roofing systems;
- and
- there are upgrades to the structure's thermal proportion (when necessary).

The Consultant must prepare a report on the current condition of the property that categorically examines the structure utilizing a 35 point checklist. The Consultant must determine the repairs/improvements that are required to meet the U.S Department of Housing and Urban Development (HUD's) Minimum Property Requirements, Minimum Property Standards and local requirements. The report must address any deficiencies that exist. The Consultant is responsible for identifying all required architectural exhibits. The Consultant must prepare the exhibits, or, if not qualified to prepare all of the necessary exhibits, must obtain the exhibits from a qualified subcontractor.

The Consultant must prepare an unbiased Work Write-up and Cost Estimate without using a contractor's estimate. The Work Write-Up and Cost Estimate must be detailed as to the work being performed based on the project proposal, including all required reports.

The Consultant must physically inspect the work for completion, quality of workmanship, conformity to local codes and ordinances, and ensure that all building permits are onsite for the work that was performed at each draw request.

At the Borrower's or Mortgagee's request, the Consultant must review proposed changes to the Work Write-Up and prepare a Change Order Form HUD-95277. The Consultant must inform the Mortgagee of the progress of the rehabilitation and of any problems that arise, including:

- work stoppages for more than 30 consecutive days or work not progressing;
- significant deviations from the Work Write-Up without the Consultant's approval;
- any issues that could affect adherence to the program requirements or property eligibility; or
- any issues that could affect the health and safety of the occupants or the security of the structure.

The Borrower is responsible for the fee charged by the Section 203(k) Consultant. Under the Standard 203(k) program, the Consultant fee charged for the Feasibility Study, Work Write-Up, Mileage (not associated with a Draw inspection) and Architectural Exhibit preparation, may be included in the mortgage as a part of the cost of rehabilitation.

III. Section 203(k) Consultants Fee Schedule

Under the existing structure, the fee is based on a range of repair costs, recognizing that more extensive repairs would require more time and are costlier for the Consultant to complete. It also allows for some level of change over time as repair costs increase. HUD establishes and monitors the maximum fees that a Section 203(k) Consultant may charge a Borrower to prepare the Work Write-Up for repairs associated with the Section 203(k) mortgage. The Work Write-Up includes the initial inspection, Architectural Exhibit Review and Cost Estimate. The current fee schedule, which HUD issued in 1995, is as follows:

| Maximum Consultant Fee | Cost of Repairs | Maximum Amount that can be Financed |
|---|--------------------------------|--|
| 203(k) Consultant Fee Schedule for preparing the Work Write-up | | |
| \$400 | Less than \$7,500 | \$ 400 |
| \$500 | Between \$7,501 and \$15,000 | \$ 500 |
| \$600 | Between \$15,001 and \$30,000 | \$ 600 |
| \$700 | Between \$30,001 and \$50,000 | \$ 700 |
| \$800 | Between \$50,001 and \$75,000 | \$ 800 |
| \$900 | Between \$75,001 and \$100,000 | \$ 900 |

| | | |
|---|---|---------|
| \$1,000 | Above \$100,000 | \$1,000 |
| Plus an additional \$25 for each additional Dwelling Unit, not to exceed \$75 | | |
| The 203(k) Roster Consultant may charge a fee for additional services listed below: | | |
| \$100 | Feasibility Study (if one is performed) | \$100 |
| \$100 | For Preparing a Change Order Request | \$100 |
| \$50 | For each Re-Inspection requested | \$50 |

The 203(k) Roster Consultant may also charge a reasonable and customary fee, not to exceed \$350 for each draw inspection request plus mileage at the current Internal Revenue Service mileage rate when the place of business is more than 15 miles from the property.

HUD has determined that the existing fee structure may discourage Consultant participation in the Section 203(k) Program and has the potential to limit access to credit. Between 2012 and 2015, the volume of loans requiring the use of a Consultant fell from 6,753 to 5,359. Based on the first two quarters of 2016, the projected volume of loans requiring the use of a Consultant is 5,132, while the projected volume of loans not requiring the use of a Consultant is 14,224. This data suggests that Borrowers are choosing the less complicated repair work, not requiring a Consultant. HUD believes that establishing a fee structure that is more in alignment with market rates would increase Consultants' participation in the Section 203(k) program and expand access to credit by encouraging and enabling more Borrowers to purchase properties that require substantial rehabilitation. The willingness and ability of Borrowers to purchase properties involving substantial rehabilitation would contribute to the reduction in build-up of HUD's Real Estate Owned inventories, result in an increase in energy efficient homes and assist in the stabilization of the housing market.

As part of its policy consolidation effort, HUD posted on the Single Family Housing Policy Drafting Table¹ its draft 203(k) Consultant Product Sheet section of the Single Family

¹ See, http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/SFH_policy_drafts.

Policy Handbook 4000.1 and requested comments.² The feedback that HUD received was that the fee schedule is not in alignment with current market rates and needs to be revised. Most commenters stated that the fee schedule was out-of-date and did not reflect the current cost of business. For example, some commenters stated that Consultants are dealing with issues like mold, radon, and other environmental hazards that were not widely recognized as issues in 1995 when HUD issued the current fee schedule. In addition, the feedback questioned the structure of the current fee schedule. For example, one commenter stated that the Consultant is limited to charging the same fee whether the home is 4,100 square feet with a crawlspace or 1,200 square feet on a slab.

IV. Request for Public Comments on Updating the Section 203(k) Consultant Fee Schedule

In order to better inform HUD, this notice seeks public comment on ways to revise the fee schedule for 203(k) Consultants. HUD is specifically seeking information to determine whether Consultant fees should continue to be based on the total cost of repairs or on some other metric. While all comments on updating the Consultant fee schedule are welcome, HUD is soliciting specific comments on the following options:

1. Retain the current fee structure but update maximum fees. Under this option, HUD would continue to base Consultant fees on the total cost of repairs and continue to allow Borrowers the ability to finance all fees into the 203(k) mortgage. If HUD uses this option, should it continue to use the current ranges for cost of repair, and if not, how should HUD set these thresholds and why? What should be the maximum Consultant fee at each threshold and why? Should the fees be tied to Consumer Price Index to account for regional differences in the cost of services?

² See, http://portal.hud.gov/hudportal/documents/huddoc?id=SFH_POLI_203K_CSL.PDF.

2. Allow Consultants to charge fees that are reasonable and customary. Under this option, Consultants would be allowed to charge fees that are reasonable and customary in the market for similar work performed by professionals with similar qualifications. If HUD uses this option, how can it manage risk associated with this concept? Should HUD continue to permit all fees to be financed or should it establish a maximum amount that can be financed in the 203(k) loan? If HUD uses this option what should be used to establish the financeable portion of the fee? Would requiring the Borrower to pay the excess fees adversely limit the number of Section 203(k) loan origination? Would this method of setting fees lead to an increase in the number of loans with negative equity? Would this method of setting fees lead to an increase in the number of loans with negative equity and how could HUD protect against this?

3. Develop a different metric on which to base Consultant fees. Under this option, Consultants' fees would be based on a metric other than cost of repairs. For example, HUD could set fees based on a straight percentage of the repair amount or a fixed fee plus a percentage of the repair amount. If HUD uses this option, at what level should HUD set the amount? Would this option allow for regional differences in the cost of services or in the variation and complexity of services provided in a specific loan transaction? Are there other metrics upon which HUD could base Consultant fees? If so, what are the pros and cons of each metric?

4. Index Section 203(k) Consultant fees to another measure. Under this option, Consultant fees could be tied to Consumer Price Index or the Annual Rate of Inflation. HUD could then revise the fees under such measure and alert the public by Mortgagee Letter or Handbook publication. What are the pros and cons of tying the 203(k) Consultant fee schedule to either of these two measures? Are there other measures that would more accurately establish

maximum fees? Would there be any reason for HUD to establish a maximum amount of the fee that can be financed into the 203(k) mortgage using either of these measures?

Dated: August 26, 2016

Edward L. Golding,
Principal Deputy Assistant Secretary for Housing

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